71

53561a

(4)

37 pgs

FILED
NOV 1 - 2007
OFFICE OF THE CLERK
SUPREME COURT, U.S.

No. 06-1463

IN THE

Supreme Court of the United States

ARNOLD M. PRESTON,

Petitioner,

v.

ALEX E. FERRER,

Respondent.

On Writ of Certiorari
to the Court of Appeal of California,
Second Appellate District

BRIEF OF MACY'S GROUP INC. AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

HARRY I. JOHNSON III
JONES DAY
555 South Flower
Street, 50th floor
Los Angeles, CA 90071
(213) 489-3939

GLEN D. NAGER
(*Counsel of Record*)
C. KEVIN MARSHALL
JONES DAY
51 Louisiana Avenue, N.W.
Washington, DC 20001
(202) 879-3939
Counsel for Amicus Curiae

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20002

QUESTION PRESENTED

Whether the Federal Arbitration Act and *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440 (2006), pre-empt the holding of the California Court of Appeal in this case that voided an interstate arbitration agreement under the California Talent Agencies Act?

TABLE OF CONTENTS

Page

QUESTION PRESENTED i

TABLE OF AUTHORITIES iv

STATEMENT OF INTEREST 1

SUMMARY OF ARGUMENT 2

ARGUMENT 3

I. THE FAA AND SUPREMACY CLAUSE REQUIRE STATE COURTS TO PUT ARBITRATION AGREEMENTS ON "THE SAME FOOTING AS OTHER CONTRACTS," AND THEREBY PROHIBIT STATES FROM PIECEMEAL OR *DE FACTO* VOIDING OF SUCH AGREEMENTS OUT OF HOSTILITY FOR ARBITRATION 3

A. Section 2 of the FAA establishes a strong federal policy in favor of enforcing arbitration agreements according to their terms, just like other contracts—a policy that applies to arbitration of statutory rights and pre-empts contrary state policy 3

B. Section 2's pre-emptive mandate prohibits state courts from piecemeal or *de facto* voiding of arbitration agreements out of hostility for arbitration, just as much as it prohibits States from directly voiding them 10

TABLE OF CONTENTS
(Continued)

Page

II. THIS COURT, IN REVERSING THE DECISION BELOW, SHOULD REITERATE THE FAA'S PRE-EMPTIVE EQUAL-FOOTING MANDATE FOR CALIFORNIA COURTS, WHICH ARE INFECTED WITH GROWING HOSTILITY TOWARD THE TERMS OF ARBITRATION AGREEMENTS INVOLVING INDIVIDUALS. 15

A. This Court repeatedly has had to check the hostility of California courts toward arbitration involving individuals. 16

B. The decision below is part of a series of recent California decisions revealing more explicit hostility to arbitration involving individuals 20

C. This trend in the California courts is important, is openly at odds with this Court's precedents under the FAA, and merits the Court's attention in deciding this case 24

CONCLUSION 31

TABLE OF AUTHORITIES

Page

Cases

Allied-Bruce Terminix Cos. v. Dobson,
513 U.S. 265 (1995) ..... *passim*

Armendariz v. Found. Health Psychcare Servs., Inc., 24 Cal. 4th 83 (2000) ..... *passim*

Buckeye Check Cashing, Inc. v. Cardegna,
546 U.S. 440 (2006) 5, 16, 17, 20, 24

Circuit City Stores, Inc. v. Adams,
532 U.S. 105 (2001) ..... *passim*

Dean Witter Reynolds, Inc. v. Byrd,
470 U.S. 213 (1985) 5, 6

Discover Bank v. Superior Court,
36 Cal. 4th 148 (2005) 20, 22, 23

Discover Bank v. Superior Court,
129 Cal. Rptr. 2d 393 (Ct. App. 2003) 26, 27

Doctor's Assocs., Inc. v. Casarotto,
517 U.S. 681 (1996) 5, 11, 12, 13, 26

EEOC v. Waffle House, Inc.,
534 U.S. 279 (2002) 5

Ferrer v. Preston, 145 Cal. App. 4th 440 (2006) 16

First Options of Chicago, Inc. v. Kaplan,
514 U.S. 938 (1995) 5

Gentry v. Superior Court,
42 Cal. 4th 443 (2007) ..... *passim*

Gilmer v. Interstate/Johnson Lane Corp.,
500 U.S. 20 (1991) 5, 8, 9, 20, 27, 28

TABLE OF AUTHORITIES
(Continued)

Page

Green Tree Fin. Corp.-Ala. v. Randolph, 531 U.S. 79 (2000) ..... *passim*

Little v. Auto Steigler, Inc., 29 Cal. 4th 1064 (2003) 24

Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52 (1995) 13, 15, 19, 28

Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc., 473 U.S. 614 (1985) ..... *passim*

Moses H. Cone Mem. Hosp. v. Mercury Constr. Corp., 460 U.S. 1 (1983) 18

Perry v. Thomas, 482 U.S. 483 (1987) ..... *passim*

Rodriguez de Quijas v. Shearson/Am. Express, Inc., 490 U.S. 477 (1989) 8, 25, 28, 29, 30

Shearson/Am. Express, Inc. v. McMahon, 482 U.S. 220 (1987) 7, 18

Southland Corp. v. Keating, 465 U.S. 1 (1984) ..... *passim*

Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Jr. Univ., 489 U.S. 468 (1989) ..... *passim*

Wilko v. Swan, 346 U.S. 427 (1953) 8, 10, 25, 29

Federal Statutes

Federal Arbitration Act, § 2, 9 U.S.C. § 2 ..... *passim*

STATEMENT OF INTEREST*

Amicus Macy's Group Inc. is a department store holding company whose stores include Macy's and Bloomingdale's. Formerly known as Federated Department Stores, Inc., it has had a workplace dispute resolution program in all of its divisions since 2003. Information regarding the program is provided to all employees through multiple channels. The final step of this program involves binding arbitration, although employees are given the opportunity to opt out of that final step without any negative impact on their employment. Arbitration is administered by the American Arbitration Association and allows ample discovery.

Amicus has a particular interest in this case because it has thousands of employees in California who are part of the dispute resolution program. Macy's Group therefore depends on the courts of that State properly enforcing arbitration agreements according to their terms, as the Federal Arbitration Act ("FAA") requires.

---

* The parties have consented to the filing of this brief; letters of consent are on file with the Clerk of the Court. No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than the *amicus curiae*, its employees, or its counsel made a monetary contribution to its preparation or submission.

SUMMARY OF ARGUMENT

Section 2 of the FAA establishes a strong federal policy in favor of enforcing arbitration agreements on an equal footing with other contracts, and thus requires enforcing them according to their terms. Equally well established is that that policy applies to arbitration of statutory rights and that, pursuant to the Supremacy Clause, it pre-empts any contrary state policy. Furthermore, the pre-emptive mandate of Section 2 not only bars state courts from directly voiding arbitration agreements out of hostility for arbitration but also prohibits them from piecemeal or *de facto* voiding of such agreements.

These basic propositions, reaffirmed repeatedly by this Court, are under siege in the courts of California, the decision below being just one in a long line of cases revealing hostility to arbitration involving individuals. This trend in California courts, which has been growing, is important, is openly at odds with this Court's precedents under the FAA, and merits the Court's attention in deciding this case. *Amicus* therefore, as explained more fully below, urges the Court, in reversing the decision below, broadly to reiterate the FAA's preemptive equal-footing mandate for the benefit of California courts and those who depend on the lawful enforcement of arbitration agreements in that State.

ARGUMENT

I. THE FAA AND THE SUPREMACY CLAUSE REQUIRE STATE COURTS TO PUT ARBITRATION AGREEMENTS ON "THE SAME FOOTING AS OTHER CONTRACTS," AND THEREBY PROHIBIT STATES FROM PIECEMEAL OR *DE FACTO* VOIDING OF SUCH AGREEMENTS OUT OF HOSTILITY FOR ARBITRATION.

This case is the latest in a series in which this Court has been called on to reiterate and apply the federal policy in favor of arbitration that is set out in Section 2 of the Federal Arbitration Act ("FAA"), 9 U.S.C. § 2. State judicial and legislative efforts to directly void arbitration agreements threaten this policy most blatantly, but state courts and legislatures also can effectively void such agreements piecemeal or *de facto*, such as by excising portions of an agreement or, as here, piling judicial, administrative, or other costs and delays onto any arbitration. These less direct but equally corrosive efforts to undermine the federal policy also demand this Court's attention and correction.

A. Section 2 of the FAA establishes a strong federal policy in favor of enforcing arbitration agreements according to their terms, just like other contracts—a policy that applies to arbitration of statutory rights and pre-empts contrary state policy.

1. Section 2 of the FAA requires that written agreements to arbitrate "shall be valid, irrevocable, and enforceable, save upon such grounds as exist at

law or in equity for the revocation of any contract." 9 U.S.C. § 2. The FAA "seeks broadly to overcome judicial hostility to" arbitration agreements. *Allied-Bruce Terminix Cos. v. Dobson*, 513 U.S. 265, 272 (1995). It was Congress's "response to hostility of American courts to the enforcement of arbitration agreements, a judicial disposition inherited from then-longstanding American practice." *Circuit City Stores, Inc. v. Adams*, 532 U.S. 105, 111 (2001). Congress wanted to "change th[is] antiarbitration rule" and "overcome courts' refusals to enforce agreements to arbitrate." *Allied-Bruce*, 513 U.S. at 270-71.

The Court thus has instructed that the FAA should be interpreted with this policy favoring enforcement of arbitration agreements in mind. *See id.* at 272. For example, in *Green Tree Financial Corp.-Alabama v. Randolph*, 531 U.S. 79 (2000), in "considering whether respondent's agreement to arbitrate [wa]s unenforceable" because it might impose prohibitive costs on a consumer, the Court did so "mindful of the FAA's purpose to reverse the longstanding judicial hostility to arbitration agreements and to place arbitration agreements upon the same footing as other contracts." *Id.* at 89 (internal quotation marks and ellipsis omitted).

This Court repeatedly has explained that, to accomplish this federal policy in favor of arbitration agreements, Congress through Section 2 directed that courts "place such agreements upon *the same footing as other contracts.*" *Volt Info. Scis., Inc. v. Bd. of Trs. of Leland Stanford Jr. Univ.*, 489 U.S. 468, 474 (1989) (internal quotation marks omitted); *Gilmer v. Interstate/Johnson Lane Corp.*, 500 U.S.

20, 24 (1991) (FAA's purpose was "to place arbitration agreements upon the same footing as other contracts."); *Allied-Bruce*, 513 U.S. at 271 ("same footing") (internal quotation marks omitted). More recently, the Court has referred to Section 2's "equal footing" requirement. *EEOC v. Waffle House, Inc.*, 534 U.S. 279, 293 (2002) (The "FAA directs courts to place arbitration agreements on equal footing with other contracts."); *Buckeye Check Cashing, Inc. v. Cardegna*, 546 U.S. 440, 443 (2006) ("Section 2 . . . places arbitration agreements on equal footing with all other contracts.").

The simple but powerful rule following from Section 2's equal-footing mandate is that courts must enforce "private agreements to arbitrate . . . according to their terms," just like other contracts. *Doctor's Assocs., Inc. v. Casarotto*, 517 U.S. 681, 688 (1996) (internal quotation marks omitted); *see also, e.g., Volt*, 489 U.S. at 479 (FAA's "primary purpose" is "ensuring that private agreements to arbitrate are enforced according to their terms."); *First Options of Chicago, Inc. v. Kaplan*, 514 U.S. 938, 947 (1995) (FAA's "basic objective" is "to ensure that commercial arbitration agreements, like other contracts, are enforced according to their terms and according to the intentions of the parties.") (internal quotation marks and citations omitted). Thus, this Court in *Waffle House* declined to "reach a result inconsistent with the plain text of the contract," rejecting an argument that a government agency—not a party to the arbitration agreement—should not be able to do for a party what the party could not, pursuant to the agreement, do on his own. 534 U.S. at 294. And in *Dean Witter Reynolds, Inc. v. Byrd*, 470 U.S. 213

(1985), the Court held that, when a complaint raised claims that were arbitrable under the parties' arbitration agreements while other claims were not, a district court could not refuse to compel arbitration on the ground that it would produce inefficient duplication. Rather, the "preeminent concern of Congress in passing the Act was to enforce private agreements into which parties had entered, and that concern requires that we rigorously enforce agreements to arbitrate, even if the result is 'piecemeal' litigation, at least absent a countervailing policy manifested in another federal statute." *Id.* at 221.

2. Unlike a State, Congress could, as *Dean Witter* suggested, enact a "countervailing policy" that overrode in some area the FAA's mandate to rigorously enforce arbitration agreements according to their terms, on the same footing as any other contract. But the strength of the policy of the FAA is such that this Court over the last twenty-five years repeatedly has declined to find any such countervailing policy in federal statutes, and even has overruled the one earlier contrary precedent.

First, in *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614 (1985), the Court in an antitrust case between a foreign automaker and a domestic dealer rejected the blanket claim that, absent a clear statement in the arbitration agreement, "a court may not construe an arbitration agreement to encompass claims arising out of statutes designed to protect a class to which the party resisting arbitration belongs." *Id.* at 625. The Court could "find no warrant in" Section 2 for such a "presumption against arbitration." *Id.*

Rather, "we are well past the time when judicial suspicion of the desirability of arbitration and of the competence of arbitral tribunals inhibited the development of arbitration." *Id.* at 626-27. Absent "compelling considerations" that would provide grounds "'for the revocation of any contract,'" the FAA provided "no basis for disfavoring agreements to arbitrate statutory claims by skewing the otherwise hospitable inquiry into arbitrability." *Id.* at 627 (quoting 9 U.S.C. § 2). That was because "agreeing to arbitrate a statutory claim" did not amount to "forgo[ing] one's substantive rights under the statute," but rather just changed the forum. *Id.* at 628. Having thus interpreted the contract at issue to provide for arbitration of claims under the Sherman Act, the Court went on to enforce the arbitration agreement, rejecting the circuit court's refusal to do so based on, among other things, the public interest in enforcement of antitrust law, concern for the dealer's having to arbitrate in Japan, the arbitration agreement's having been part of a contract of adhesion, and skepticism over the likely quality of the arbitrators. *Id.* at 629, 632-34.

Mitsubishi set a firm pattern that this Court consistently has followed. In *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220 (1987) ("*McMahon*"), the Court enforced an arbitration agreement between a brokerage firm and its customer that would require arbitration of claims under the Securities Exchange Act of 1934 and the Racketeer Influenced and Corrupt Organizations Act. The Court rejected the public policy considerations on which the lower courts had relied, reiterated its rejection in *Mitsubishi* of various forms of hostility to

arbitration, *id.* at 231-32, 239-40, and concluded that the terms of the agreement controlled.

Two years later, in *Rodriguez de Quijas v. Shearson/American Express, Inc.*, 490 U.S. 477 (1989), the Court overruled *Wilko v. Swan*, 346 U.S. 427 (1953), which had barred arbitration of certain claims under the Securities Act of 1933. *Wilko* wrongly "rested on suspicion of arbitration as a method of weakening the protections afforded in the substantive law to would-be complainants." 490 U.S. at 481.

Two years after that, in *Gilmer*, the Court held that a claim under the federal Age Discrimination in Employment Act was subject to arbitration under an employee's arbitration agreement. The Court reiterated *Mitsubishi*'s recognition that an agreement to arbitrate a statutory claim merely changes the forum and thus "does not forgo the substantive rights." 500 U.S. at 26 (internal quotation marks omitted). The Court also rejected "a host of challenges to the adequacy of arbitration procedures" that were laced with "generalized attacks on arbitration" already rejected in *Rodriguez*. *Id.* at 30. Finally, the Court rejected an argument based on "unequal bargaining power between employers and employees," seeing no warrant under Section 2's "same footing" requirement for disregarding the agreement absent coercion, fraud, or some similar ground applicable to any contract. *Id.* at 33.

Most recently, in *Randolph*, the Court applied these cases to the question whether, even assuming Congress had no intention of requiring a judicial forum for a federal statutory claim, an arbitration agreement still could be unenforceable on the ground

that arbitration would be financially prohibitive for a party. That claimed risk was "too speculative to justify the invalidation," 531 U.S. at 91, and at odds with the "liberal federal policy favoring arbitration agreements," *id.* (internal quotation marks omitted). The Court put the burden on the party challenging the agreement to show, with evidence, that she would bear the costs and that those costs would be prohibitive for her. *Id.* at 91-92.

All of these cases were but particular applications of the FAA's broad purpose of reversing judicial hostility to arbitration agreements. *See id.* at 89-90 (summarizing). They "demonstrate that even claims arising under a statute designed to further important social policies may be arbitrated because '"so long as the prospective litigant effectively may vindicate [his or her] statutory cause of action in the arbitral forum,"' the statute serves its functions." *Id.* at 90 (quoting *Gilmer*, 500 U.S. at 28, in turn quoting *Mitsubishi*, 473 U.S. at 637; alterations in *Randolph*).

3. All the more does the federal policy in favor of arbitration apply to States, who, unlike Congress, have no authority given the Supremacy Clause to enact, apply, or enforce some contrary policy, particularly one involving hostility to arbitration. The Court first held the FAA applicable in state court in *Southland Corp. v. Keating*, 465 U.S. 1 (1984); reaffirmed this holding in *Allied-Bruce* eleven years later; and thus recently has explained that the FAA is "applicable in state courts, and pre-emptive of *state laws hostile to arbitration*," *Circuit City*, 532 U.S. at 112 (emphasis added). Thus, for example, an intention on the part of a State "to preclude a waiver of judicial remedies for [certain] statutory rights"

could not override the FAA, even though this Court in considering *federal* statutory rights does "ask whether Congress has evinced [such] an intention." *Randolph*, 531 U.S. at 90.

Indeed, *Southland* specifically contrasted the freedom of Congress, if it wished, to vary the application of the FAA for policy reasons with the lack of authority of States to do so. The state court's reliance on *Wilko* was "unpersuasive" because it overlooked this constitutional distinction. 465 U.S. at 16 n.11. In state court, even more than federal, objections to full enforcement of arbitration agreements must rest on "general contract defenses such as fraud," not on laws or policies hostile or otherwise specific to arbitration. *Id.*

And in *Circuit City*, which held that Section 1 does not exclude all employment contracts from the FAA (but rather just employment contracts involving transportation workers), the Court rejected the pleas of 21 States that such a holding "intrudes upon the policies of the separate States" in their "traditional role in regulating employment relationships." 532 U.S. at 121-22. Such was the inevitable result, under *Southland* and *Allied-Bruce*, of applying an ordinary interpretation of the text of Section 1, and did not justify distorting the law. *Id.* at 122.

B. Section 2's pre-emptive mandate prohibits state courts from piecemeal or *de facto* voiding of arbitration agreements out of hostility for arbitration, just as much as it prohibits States from directly voiding them.

The most basic violation of the FAA is to decline to enforce an arbitration agreement at all.

Thus, the Court has said, referring to the old judicial hostility, that "the basic purpose of the [FAA] is to overcome courts' refusals to enforce agreements to arbitrate." *Allied-Bruce*, 513 U.S. at 270. Petitioner claims that California did just that in the decision below, invalidating the agreement "by inserting an administrative proceeding ahead of a decision by the Courts," Pet. 6, although Respondent disputes that claim, Opp. 4. Beyond that point, however, is the corollary that a court also can be "hostile to arbitration," *Circuit City*, 532 U.S. at 112, and "undercut the enforceability of arbitration agreements," *Southland*, 465 U.S. at 16, by piecemeal or *de facto* voiding of arbitration agreements.

The FAA prohibits indirect as well as direct means of voiding or refusing to enforce arbitration agreements. The overriding question under the FAA, particularly in reviewing actions of state courts, is whether the applicable law or rule targets arbitration agreements for treatment that is special or different from other contracts, because such arbitration-specific law "would place arbitration clauses on an unequal 'footing,' directly contrary to the [FAA's] language and Congress's intent." *Doctor's Assocs.*, 517 U.S. at 686 (internal quotation marks omitted). When a court declines fully to apply an arbitration agreement according to its terms, and does so for reasons hostile or otherwise specific to arbitration, it violates the FAA.

Allied-Bruce and *Doctor's Associates* together illustrate this point. In the former, the Court straightforwardly applied the FAA to a state statute that, equally straightforwardly, made pre-dispute arbitration agreements invalid and unenforceable.

See Allied-Bruce, 513 U.S. at 269. The Court set out a simple rule:

> States may regulate contracts, including arbitration clauses, under general contract law principles and they may invalidate an arbitration clause "upon such grounds as exist at law or in equity for the revocation of *any* contract." 9 U.S.C. § 2 (emphasis added). What States may not do is decide that a contract is fair enough to enforce all its basic terms (price, service, credit), but not fair enough to enforce its arbitration clause. The Act makes any such state policy unlawful.

Id. at 281.

The next year in *Doctor's Associates*, the Court applied this rule to a Montana law that, rather than making arbitration agreements invalid, just imposed special conditions for enforcement: The first page of any contract subject to arbitration had to refer to the arbitration provision in underlined capital letters. 517 U.S. at 683. "Congress precluded states from *singling out arbitration provisions for suspect status*," yet the State had "condition[ed] the enforceability of arbitration agreements on compliance with a special notice requirement not applicable to contracts generally." *Id.* at 687 (emphasis added). More generally, the Court explained, quoting a treatise, prior cases stood for the rule that "state legislation requiring greater information or choice in the making of agreements to arbitrate than in other contracts is preempted." *Id.* (internal quotation marks omitted). States remained

free, however, to apply general contract defenses "such as fraud, duress, or unconscionability." *Id.*

Volt illustrates the same principle. The lower court had imposed a stay of arbitration pending the resolution of related litigation, applying a state law providing for such a stay. This Court affirmed, but only by concluding that the parties in their arbitration agreement had incorporated the state law that authorized such a stay. *See* 489 U.S. at 476-77. The FAA did not pre-empt the state law, but only because the state law applied according to the terms of the agreement. The Court reiterated this understanding in *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52 (1995), when, drawing on *Volt*, *Allied-Bruce*, and other cases, it made clear that the FAA would pre-empt both a state law that *prohibited* the parties from including claims for punitive damages within the issues to be arbitrated, and likewise a state law that *required* the parties to include punitive damages notwithstanding the terms of their agreement. *See id.* at 58.

Mitsubishi illustrates (in a case coming from federal rather than state court) the same approach of barring special conditions on arbitration not part of the arbitration agreement. The court rejected a clear-statement rule for applying arbitration agreements to statutory rights, *see* 473 U.S. at 624-25, and also rejected an approach to enforceability that involved special skepticism for arbitration agreements that were contracts of adhesion or applied to an antitrust suit. *Id.* at 655-56. The Court thus recognized that hostility to arbitration might appear not only in a general refusal to enforce agreements but also in a willingness to enforce them

as a general matter while in particular areas declining to enforce them or imposing special requirements. The FAA bars state courts from this more selective manifestation of hostility as well: *Southland* found pre-empted a provision in a state franchise law that exempted from arbitration claims arising under that law, 465 U.S. at 5, and *Perry v. Thomas*, 482 U.S. 483, 484 (1987), held pre-empted a state law exempting wage claims from arbitration.

Perry set out in detail both the permissibility and the limits of state law under the FAA's "same footing" doctrine, and established that the doctrine applied to judge-made rules just as much as to statutory rules. The Court declined to address a question of unconscionability not decided in the courts below, but nevertheless provided directions for remand: Because under Section 2 an agreement only may be voided under general contract law, "state law, whether of legislative or judicial origin, is applicable *if* that law arose to govern issues concerning the validity, revocability, and enforceability of contracts generally. A state-law principle that *takes its meaning precisely from the fact that a contract to arbitrate is at issue*" violates Section 2. 482 U.S. at 492 n.9 (second emphasis added). A court "may not," therefore,

> in assessing the rights of litigants to enforce an arbitration agreement, construe that agreement in a manner different from that in which it otherwise construes nonarbitration agreements under state law. Nor may a court rely on the uniqueness of an agreement to arbitrate as a basis for a state-law

> holding that enforcement would be unconscionable, for this would enable the court to effect what we hold today the state legislature cannot.

Id. In other words, even though state law generally governs the interpretation of arbitration agreements just as it would any other contract, *see Volt*, 489 U.S. at 474; *Mastrobuono*, 514 U.S. at 60 n.4, that state contract law must truly be "general," rather than targeting arbitration or otherwise manifesting hostility toward it.

II. THIS COURT, IN REVERSING THE DECISION BELOW, SHOULD REITERATE THE FAA'S PRE-EMPTIVE EQUAL-FOOTING MANDATE FOR CALIFORNIA COURTS, WHICH ARE INFECTED WITH GROWING HOSTILITY TOWARD THE TERMS OF ARBITRATION AGREEMENTS INVOLVING INDIVIDUALS.

Notwithstanding the clear and repeated admonitions of this Court, based on Section 2 of the FAA, to dispense with hostility toward arbitration and to enforce arbitration agreements rigorously according to their terms, on the same footing as any other contract, the courts in California have continued to harbor and carry out a pervasive hostility to arbitration agreements involving individuals, particularly in the area of employment contracts. That open hostility undermines this Court's precedents, creates harmful uncertainty for those with such agreements in that major State, and merits the Court's attention in this case.

A. This Court repeatedly has had to check the hostility of California courts toward arbitration involving individuals.

The present case is the latest in a long line coming to this Court out of California, and is not unusual in the starkness of its disregard of the FAA and this Court's precedents. In February 2006, this Court in *Buckeye Check Cashing* held that Section 2, together with the rule that arbitrators decide the validity of contracts subject to arbitration (as distinct from the validity of arbitration agreements), barred a State from refusing to compel arbitration on the ground that a loan contract containing an arbitration agreement was illegal and even criminal under various state lending and consumer-protection laws. *See* 546 U.S. at 443, 445-46. The Court directly rejected the Florida Supreme Court's reliance on state public policy and explained that *Southland* "rejected the proposition that the enforceability of the arbitration agreement turned on the state legislature's judgment concerning the forum for enforcement of the state-law cause of action." *Id.* at 447. Barely nine months later, a divided panel of the California Court of Appeal, in the decision below, affirmed a trial court ruling declining to enforce an arbitration agreement and instead interpreting a state statute as requiring initial resort to a state administrative forum. *Ferrer v. Preston*, 145 Cal. App. 4th 440, 444-46 (2006). In a single paragraph, the Court of Appeal summarily disregarded *Buckeye Check Cashing* on its facts, as well as the dissent's arguments based on the case, ignoring the broad basis of the decision. *Id.* at 447.

This approach continues a pattern that stretches back at least to *Southland*, one of the two primary authorities on which *Buckeye Check Cashing* relied. The California Supreme Court in *Southland* had held that the California Franchise Investment Law, in barring any "waive[r]" by individual franchisees of "compliance with any provision of" that law, required judicial consideration of claims and thus barred enforcement of an agreement to arbitrate them. 465 U.S. at 10 (internal quotation marks omitted). This Court saw "nothing in the Act indicating that the broad principle of enforceability is subject to any . . . limitations under State law" beyond those that Section 2 indicated. *Id.* at 11. It thus held that the state law violated the Supremacy Clause, and explained that in the FAA "Congress intended to foreclose any state legislative attempts to undercut the enforceability of arbitration agreements." *Id.* at 16. Under Section 2, States only may use "general contract defenses such as fraud to avoid enforcement of an arbitration agreement," yet the California law did not involve such a defense. While Congress might provide for such a defense to arbitration as the franchise law set out, California could not. *Id.* at 16 n.11.

Three years later in *Perry*, this Court again corrected the California courts' open refusal to follow the FAA. A provision of the California Labor Code provided that lawsuits to collect wages could be maintained "without regard to the existence of any private agreement to arbitrate." 482 U.S. at 484 (internal quotation marks omitted). The trial court, applying it, had denied a petition to compel

arbitration of an employee's breach-of-contract claim. The Court of Appeal affirmed in an unpublished opinion, and the California Supreme Court denied review. *Id.* at 488-89. In holding that the FAA pre-empted the state provision, this Court began with this broad admonition: "'Section 2 is a congressional declaration of a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary.'" *Id.* at 489 (quoting *Moses H. Cone Mem. Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1, 24 (1983)). The Court also reiterated *Southland*'s rejection of any state-law limitation on enforceability of an arbitration agreements apart from those that Section 2 indicated, as well as its concluding explanation that the FAA "'intended to foreclose state legislative attempts to undercut the enforceability of arbitration agreements.'" *Id.* at 489-90 (quoting *Southland*, 465 U.S. at 11 & 16, respectively). And the Court emphasized the mandate, as set out in *McMahon*, to rigorously enforce arbitration agreements. *Id.* at 490. The California law was "in unmistakable conflict" with the "clear federal policy." *Id.* at 491.

Volt did, in a suit between a university and a construction company, affirm a decision of the California Supreme Court applying California's statutory arbitration procedures, including a stay of arbitration. But, as explained above, this Court did so only on the theory that the parties had, by agreeing to apply California law, agreed to apply California's arbitration statute. 489 U.S. at 476. The Court thus emphasized not any deference to state law or particular arbitration procedures, but rather the basic federal policy under Section 2 of "ensur[ing] the

enforceability, according to their terms, of private agreements to arbitrate." *Id.*; *see id.* at 478 (similar). *Southland* and *Perry*, the Court explained, did not establish that the FAA "prevents the enforcement of agreements to arbitrate under different rules than those set forth in the Act itself," but rather were, just like the decision in *Volt* itself, manifestations of "the FAA's primary purpose of ensuring that private agreements to arbitrate are enforced according to their terms," including terms that "specify by contract the rules under which that arbitration will be conducted." *Id.* at 479. Furthermore, the Court in *Mastrobuono* indicated that it considered the California Supreme Court's interpretation of the parties' agreement in *Volt*, to incorporate state arbitration procedure, as at the outer edge of plausibility. *See* 514 U.S. at 60 n.4.

Finally, *Circuit City*, although coming to this Court from California federal rather than state court, involved a similar scenario to *Southland* and *Perry*. After all eight circuits to consider the question had held that Section 1 of the FAA excluded from the FAA's coverage only employment contracts of transportation workers, the Ninth Circuit held that Section 1 excluded *all* employment contracts. 532 U.S. at 110-11. In a case involving an employment contract of a Circuit City employee in California, this Court reversed the Ninth Circuit. The Court pointedly opened by noting that "[a]ll but one of the Courts of Appeals which have addressed the issue" agreed with the Court's interpretation of Section 1. *Id.* at 109. The Court reiterated that the FAA was "pre-emptive of state laws hostile to arbitration," *id.* at 112, and concluded by specially rejecting the plea

of 21 States to follow the Ninth Circuit's reading. *Id.* at 121-22. Citing *Gilmer*, the Court explained, "We have been clear in rejecting the supposition that the advantages of the arbitration process somehow disappear when transferred to the employment context." *Id.* at 123.

B. The decision below is part of a series of recent California decisions revealing more explicit hostility to arbitration involving individuals.

The hostility of California courts to arbitration involving individuals, and to this Court's holdings and admonitions under the FAA, has been hardly limited to the cursory dismissal of the FAA and *Buckeye Check Cashing* by the court below. Rather, it appears persistently in a series of recent decisions by the California Supreme Court, most notably *Gentry v. Superior Court*, 42 Cal. 4th 443 (2007); *Discover Bank v. Superior Court*, 36 Cal. 4th 148 (2005); and *Armendariz v. Foundation Health Psychcare Services, Inc.*, 24 Cal. 4th 83 (2000). Each imposes, in disregard of the FAA's rule to rigorously enforce arbitration agreements according to their terms, yet another restriction on the ability of companies to enforce their arbitration agreements in California courts as written. The California courts are methodically whittling away at arbitration, erecting barriers to enforcement piecemeal, with the *de facto* result of making them at least practically unenforceable—contrary to Section 2, the Supremacy Clause, and this Court's precedents.

Gentry involved a claim for overtime pay pursuant to the California Labor Code, the same code at issue in *Perry*, by a former employee of Circuit City who claimed that Circuit City had misclassified

certain employees as exempt from the minimum wage. The plaintiff had, in commencing his employment, declined to opt out of an arbitration agreement that barred class arbitration, and the question was whether the waiver on class arbitration was enforceable. *See Gentry*, 42 Cal. 4th at 451. Somewhat as in *Southland* (involving an unwaivable statutory right of a franchisee), the California Supreme Court explained that "the rights to the legal minimum wage and legal overtime compensation conferred by the statute are unwaivable," that the legislature intended that "minimum wage and overtime laws should be enforced in part by private action brought by aggrieved employees," and that "overtime legislation" had great "public importance." *Id.* at 455-56 (internal quotation marks omitted). The court also pointed to a portion of the Civil Code setting out a public policy against contracts that "exempt anyone from responsibility for his own fraud, or willful injury to the person or property of another, or violation of law, whether willful or negligent." *Id.* at 453-54 (internal quotation marks omitted).

The court announced the general rule that "a class arbitration waiver" could "lead to a de facto waiver and would impermissibly interfere with employees' ability to vindicate unwaivable rights and to enforce the overtime laws." *Id.* at 457.[1] In fact, a class arbitration waiver could have such effect "at

---

[1] The term "class arbitration waiver" was used by the California Supreme Court to describe any provision in an arbitration agreement that required individual-specific arbitration of a dispute rather than class or consolidated claims.

least frequently if not invariably." *Id.* A court should "invalidate the class arbitration waiver" if it determined, based on four factors, "that a class arbitration is likely to be a significantly more effective practical means of vindicating the rights of the affected employees than individual litigation or arbitration" and "that the disallowance of the class action will likely lead to a less comprehensive enforcement of overtime laws for the employees alleged to be affected." *Id.* at 463. In practice, invalidation will be the rule, as the court merely declined to "foreclose the possibility" that some waivers in arbitration agreements could be enforced. *Id.* at 464. The court remanded for the trial court to apply this new rule, *id.* at 466, while acknowledging that, in light of it, Circuit City might no longer desire arbitration, *id.* at 467. In a separate part of the opinion, the *Gentry* court went on to pave the way for striking down as unconscionable any class-arbitration waiver that survived this gauntlet. *See id.* at 470-73.

Discover Bank was a primary authority for *Gentry*, and the California Supreme Court there effectively excised class arbitration waivers from arbitration agreements in consumer contracts. The plaintiff sought a class action against his credit card company for allegedly defrauding a large number of customers of small amounts of money. *Discover Bank*, 36 Cal. 4th at 154. The credit card company had used a "bill stuffer" to amend its agreement with customers to require arbitration of all disputes and prohibit class arbitration. The court found such agreements generally unconscionable and thus unenforceable, emphasizing state policies in favor of

class actions and class arbitrations in consumer actions. *See id.* at 156. In particular, such agreements amounted to exculpatory contract clauses in violation of the state Civil Code, at least when (1) the waiver was in a consumer contract of adhesion, (2) involving disputes likely to involve small amounts of damages, and (3) the plaintiff alleged "that the party with superior bargaining power has carried out a scheme to deliberately cheat large numbers of consumers out of individually small sums of money." *Id.* at 162-63.

Gentry also relied on *Armendariz*, which itself had imposed four preconditions for the enforcement of any pre-dispute agreement to arbitrate unwaivable statutory employment rights: (1) The arbitration agreement may not limit the damages normally available under the statute; (2) there must be discovery sufficient to adequately arbitrate the statutory claim; (3) there must be a written arbitration decision and judicial review, sufficient to ensure that the arbitrators comply with the statute, and (4) the employer must pay all types of costs that are unique to arbitration. *See Armendariz*, 24 Cal. 4th at 103, 106, 113; *see also Gentry*, 42 Cal. 4th at 456-57 (summarizing *Armendariz*). *Gentry* generally described *Armendariz* as "mak[ing] clear that for public policy reasons we will not enforce provisions contained within arbitration agreements that pose significant obstacles to the vindication of employees' statutory rights." *Gentry*, 42 Cal. 4th at 463 n.7.

Three years after *Armendariz*, the California court held unconscionable, in a suit for termination of employment in violation of public policy, "a provision in a mandatory employment arbitration agreement

that permits either party to 'appeal' an arbitration award of more than $50,000"; imposed on the remaining provisions of the arbitration agreement the four "minimum requirements for arbitration of unwaivable statutory claims" set out in *Armendariz*, and reaffirmed the final categorical requirement, regarding costs, notwithstanding this Court's intervening decision in *Randolph* that prohibitive costs must be shown, not just asserted. *Little v. Auto Stiegler, Inc.*, 29 Cal. 4th 1064, 1068-69, 1084-85 (2003).

C. This trend in the California courts is important, is openly at odds with this Court's precedents under the FAA, and merits the Court's attention in deciding this case.

In these recent California cases, including the decision below, the California courts either waved aside substantial objections based on the FAA or employed reasoning whose hostility to arbitration is indistinguishable from that which this Court has rejected in the line of cases beginning with *Mitsubishi*, or both. What the California courts did *not* do was put arbitration agreements on the same footing as other contracts and enforce them rigorously according to their terms.

This pervasive judicial hostility against arbitration involving individuals, against the FAA, and against this Court's precedents is not hidden, and it merits this Court's attention. In reversing the California Court of Appeal here, the Court should not just narrowly enforce *Buckeye Check Cashing*, but rather should more broadly reiterate and expound for the California courts, and those (such as *amicus*) with arbitration agreements in the Nation's most

populous State and largest economy, the full requirements of the FAA as set out above in Part I. *Cf. Circuit City*, 532 U.S. at 123 (rejecting proposed interpretation of FAA because, among other things, it "would call into doubt the efficacy of alternative dispute resolution procedures adopted by many of the Nation's employers, in the process undermining the FAA's proarbitration purposes" and breeding litigation).

1. Most notable among the cases showing open hostility is *Gentry*, which effectively excised prohibitions on class arbitration from arbitration agreements in employment contracts. The majority in the 4-3 decision consigned most of its discussion of the FAA to a footnote and criticized the dissent for "its preference that in this case the [*federal*] statutory policy in favor of enforcing arbitration agreements as written overrides the [*state*] statutory policy in favor of vigorously enforcing overtime laws." *Gentry*, 42 Cal. 4th at 465 n.8. This preference was not one that the California "Legislature shared or shares," nor had the Legislature "favored the arbitration of wage and overtime claims at all." *Id.* The court invoked state policy from the 1960s, *Wilko*, and a law review article arguing that Congress in enacting the FAA did not imagine its applying to "compel arbitration of statutory wage claims." *Id.* The court did briefly acknowledge that *Perry* had held the FAA pre-empted a California law barring arbitration of wage disputes, and cited *Rodriguez*, which overturned *Wilko*. *Id.* But neither concession caused the court to pause in concluding—based on *Armendariz* rather than any decision of this Court—that the FAA permits what the court called

"arbitration-neutral rules that limit enforcement of specific provisions of arbitration agreements on public policy grounds." *Id.* Yet *Armendariz* expressly set out—as *Gentry* recognized elsewhere, *id.* at 456—a set of arbitration-*specific* requirements for arbitration agreements in employment contracts. *See Armendariz*, 24 Cal. 4th at 90-91 (describing "certain minimum requirements" that an "arbitration must meet" to enable an employee to vindicate his statutory rights).

The dissenting justices in *Gentry* thus marveled that, "as the majority implicitly concedes," its authorities for legislative hostility to arbitration of wage claims all "have been *superseded or invalidated* by the prevailing public policy that *favors* enforcement of arbitration agreements according to their terms." *Gentry*, 42 Cal. 4th at 477 n.3 (Baxter, J., dissenting).

Similarly, in *Discover Bank* the California Supreme Court reversed a unanimous decision of a California Court of Appeal panel that had upheld a class action waiver in an arbitration agreement and found the FAA to "preempt[ ] a state court from applying state substantive law to strike the class action waiver from the agreement." *Discover Bank v. Superior Court*, 105 Cal. Rptr. 2d 393, 396 (Ct. App. 2003). California's public policy against class action waivers had to submit, the intermediate court reasoned, to the federal policy of enforcing arbitration agreements according to their terms. *Id.* at 403. The Court of Appeal relied on *Doctor's Associates*, the primary case in which this Court has rejected state efforts to add terms to and conditions for the

enforcement of arbitration agreements, as well as *Southland* and *Perry*. *See id.* at 404-05, 407-09.

2. The California courts' methodical superimposing of requirements or exceptions onto arbitration agreements based on state policy concerns clashes with this Court's repeated refusals to do the same when considering other *federal* laws under the FAA, as described above in Part I.A. The "generalized attacks on arbitration" by the California courts are the same ones that this Court has "already rejected," repeatedly. *Gilmer*, 500 U.S. at 30.

In *Armendariz* and *Gentry*, the California Supreme Court required "sufficient" discovery in any employment arbitration; yet in *Gilmer* this Court rejected an attack on arbitration of a federal claim of age discrimination in employment as involving overly limited discovery, *Gilmer*, 500 U.S. at 31, and in *Circuit City* this Court observed that arbitration's informality (such as reduced discovery) allows "parties to avoid the costs of litigation, a benefit that may be of particular importance in employment litigation, which often involves smaller sums of money than disputes concerning commercial contracts," 532 U.S. at 123. In *Armendariz* and *Gentry*, the California Supreme Court required that arbitrators issue a written decision; yet in *Gilmer* this Court rejected the attack that "arbitrators often will not issue written opinions," thereby depriving the public of knowledge of employment discrimination, because, among other things, judicial decisions would continue to illuminate the law and discrimination, and this concern applied equally to settlements. 500 U.S. at 31-32. In *Armendariz* and *Gentry*, the California Supreme Court outlawed

employment arbitration agreements that limit statutorily available damages; yet in *Mastrobuono* this Court indicated that the FAA leaves parties free to determine whether or not to allow punitive damages. And in *Armendariz* and *Gentry*, the California Supreme Court required the employer to pay all costs that are unique to arbitration, whereas this Court in *Randolph* refused to presume that arbitration costs would be prohibitive so as to void an arbitration agreement, and *Circuit City* recognized that arbitration can "avoid the costs of litigation," 532 U.S. at 123.

More broadly, the reasoning of California courts, in devising ways to constrain agreements by individual employees or consumers to arbitrate disputes, is suffused with "'suspicion of arbitration as a method of weakening the protections afforded in the substantive law to would-be complainants.'" *Gilmer*, 500 U.S. at 30 (quoting *Rodriguez*, 490 U.S. at 481). Yet that is the very suspicion that this Court repeatedly has rejected as barred by the FAA. As explained recently in *Circuit City*: "We have been clear in rejecting the supposition that the advantages of the arbitration process somehow disappear when transferred to the employment context. . . . [and] quite specific in holding that arbitration agreements can be enforced under the FAA without contravening the policies of congressional enactments giving employees specific protection." 532 U.S. at 123. All the more, for reasons already explained, do these propositions apply to state enactments subject to pre-emption by the FAA. *See id.* at 124.

If the encumbrances laden on arbitration by the California courts had been imposed by the state

legislature, it would be plain that the State had targeted and acted out of hostility for arbitration, and that the FAA pre-empted them. That instead the courts imposed them (usually through broad or creative applications of state statutes) makes no difference. As *Perry* recognized, Congress did "intend[ ] to foreclose state legislative attempts to undercut the enforceability of arbitration agreements," 482 U.S. at 489, but that does not mean that a court may "effect" what "the state legislature cannot," *id.* at 492 n.9.

Furthermore, California is attempting to draw to itself a policy-based power that, as this Court highlighted as early as *Southland*, 465 U.S. at 16 n.11, it does not and cannot have, one that belongs only to Congress. In this, its courts directly threaten this Court's FAA jurisprudence of the last twenty-five years. They are undercutting by degrees the enforceability of arbitration agreements involving individuals, such as in consumer and employment contracts, thereby effectively overruling this Court's decisions in *Circuit City*, *Perry*, and other cases, and warring with the reasoning of cases in the line of *Mitsubishi*. Such hostility toward precedent and federal law warrants a response from this Court, and the instant case provides a good opportunity to do so.

3. Fortunately, the grounds on which this Court could check that hostility are well established, in *Mitsubishi* and subsequent cases, as well as in the general requirements of the FAA to put arbitration agreements on an equal footing with other contracts and enforce them according to their terms. This Court's reasoning in *Rodriguez* in overturning *Wilko* may be the most instructive and applicable: The

California courts' "characterization of the arbitration process" has been "pervaded by . . . the old judicial hostility to arbitration." 490 U.S. at 480 (internal quotation marks omitted). Yet "[t]hat view has been steadily eroded over the years," particularly since *Mitsubishi*. *Id.* "To the extent that" the California courts' decisions "rest[ ] on suspicion of arbitration as a method of weakening the protections afforded in the substantive law to would-be complainants, [they have] fallen far out of step with [the Court's] current strong endorsement favoring this method of resolving disputes." *Id.*; *see also Circuit City*, 532 U.S. at 123 (discussing advantages of arbitration in employment context and its consistency with statutes protecting employees); *Randolph*, 531 U.S. at 90 (similar holding regarding "statute[s] designed to further important social policies"; refusing to indulge speculative risk that costs of arbitration would be prohibitive to consumer and preclude effectively vindicating statutory rights).

The California courts have indeed fallen far out of step with this Court, the decision below being but one small misstep in that waywardness. In correcting that particular misstep, the Court should seek more broadly to get the California courts back in step with its own precedents, the FAA, and the Supremacy Clause.

CONCLUSION

For the foregoing reasons, *amicus* respectfully urges the Court broadly to reverse the decision below.

Respectfully submitted,

GLEN D. NAGER
(*Counsel of Record*)
C. KEVIN MARSHALL
JONES DAY
51 Louisiana Avenue, N.W.
Washington, D.C. 20001
(202) 879-3939

HARRY I. JOHNSON III
JONES DAY
555 South Flower Street,
50th Floor
Los Angeles, CA 90071
(213) 489-3939

Counsel for Amicus Curiae

November 8, 2007